

**PUBLIC UTILITIES COMMISSION**

505 VAN NESS AVENUE  
SAN FRANCISCO, CA 94102-3298



December 2, 2002

**Agenda ID #1481**

**TO: PARTIES OF RECORD IN APPLICATION 02-06-019**

This is the draft decision of Administrative Law Judge (ALJ) Barnett. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. The Commission may act then, or it may postpone action until later.

When the Commission acts on the draft decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the draft decision as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's website at <http://www.cpuc.ca.gov>. Pursuant to Rule 77.3 opening comments shall not exceed 15 pages. Finally, comments must be served separately on the ALJ and the Assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service.

/s/ CAROL A. BROWN  
Carol A. Brown, Interim Chief  
Administrative Law Judge

CAB:jyc

Attachment

Decision **DRAFT DECISION OF ALJ BARNETT** (Mailed 12/2/02)**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Application of PACIFIC GAS AND ELECTRIC  
COMPANY for Authority to Increase Electric  
And Gas Revenue Requirements To Reflect An  
Attrition Revenue Adjustment For The Year 2002.  
(U 39 M)

Application 02-06-019  
(Filed June 11, 2002)

**OPINION DENYING RELIEF****Summary**

Pacific Gas and Electric Company (PG&E) requests authority to increase its base revenue requirements for electric and gas distribution, customer services, and Humboldt Nuclear SAFSTOR activities to reflect an attrition revenue adjustment (ARA) for the year 2002. PG&E requests that these revenue requirement increases be effective as of April 22, 2002.

PG&E proposes a total base revenue requirement increase of \$96.326 million, comprised of \$76.707 million for electric distribution, \$19.48 million for gas distribution, and \$0.139 million for nuclear decommissioning for Humboldt Power Plan Nuclear SAFSTOR expense. PG&E says that these increases are necessary to reflect its rate base growth due to an estimated \$1 billion in planned capital additions for 2002, as well as expense growth in such areas as wages and salaries and the costs of goods and services.

Of the total requested increase, approximately \$64 million is associated with PG&E's planned capital additions.

The Office of Ratepayer Advocates (ORA) protests PG&E's request. It argues that PG&E's attrition increases should be denied on policy grounds, should be denied because PG&E failed to file a timely application for a general rate case increase, and should be denied because a complete review of PG&E's revenues and expenses is needed before granting a rate increase.

Both PG&E and ORA agree that this proceeding can be decided without the need for a public hearing. At the prehearing conference held on September 26, 2002, the matter was submitted on the pleadings, and PG&E's Exhibits 1 and 2.

We deny the attrition increase request. In our review of PG&E's recent rate cases it is apparent that PG&E has not had a full review of its costs since its 1999 general rate case decision D.00-02-046. The recorded numbers are too stale and the escalation rates too uncertain to sustain a finding increasing rates by \$96.3 million to meet 2002 costs and rate base.

### **PG&E's Position**

PG&E states that it expects to connect approximately 61,000 new electric and 40,000 new gas customers in 2002, and that it needs to spend capital to add gas and electric distribution capacity to serve increasing loads and to maintain and replace electric and gas distribution equipment. It expects to invest \$1 billion in 2002. Without an increase in authorized revenue to pay for these investments, PG&E argues that its ability to continue to finance this level of capital additions, year to year, will be adversely affected. Absent the revenue requirement increases requested, PG&E says that it will earn significantly less than its authorized rate of return.

The ARA methodology PG&E proposes for deriving escalation rates is consistent with the 2001 ARA final decision (D.) 02-02-043; that is, PG&E applied one year of escalation (i.e. from 2001 to 2002) to previously adopted electric and gas operating expense levels. For electric operating expense, PG&E escalated the level expenses adopted in the 2001 ARA final decision; for gas operating expense, the level adopted in PG&E's 1999 GRC decision. (D.00-02-046.)

For rate base and capital-related items, PG&E derived both gas and electric 2002 rate base using the seven-year average of plant additions (for years 1994-2000 in constant dollars). For electric distribution, PG&E escalated the seven-year average of plant additions to 2002-year dollars and used the resulting number to derive the rate base growth over the rate base adopted in the 2001 ARA final decision. For gas distribution, PG&E escalated the seven-year average of plant additions to 2002-year dollars and used the resulting number to derive the rate base growth over the recorded 2001 rate base.

For its electric distribution results of operations for estimated 2002, at current rates P&GE predicts an 8.56% rate of return; at proposed rates a 9.12% rate of return. The electric rate increase requested is \$76,707,000. PG&E's authorized electric distribution rate of return is 9.12%, per D.00-06-040. See Table 1.

PACIFIC GAS AND ELECTRIC COMPANY  
2002 ATTRITION APPLICATION  
TABLE 1  
ELECTRIC DISTRIBUTION (CPUC JURISDICTION)  
RESULTS OF OPERATIONS  
(Thousands of Dollars)

Line No.	Description	2001 Attrition Decision 02-02-043	2002		Line No.
			Present Rates	Proposed Rates	
		(A)	(B)	(C)	
REVENUE:					
1	General Rate Case Revenue	2,239,676	2,239,676	2,239,676	1
2	Increase	0	0	76,707	2
3	General Rate Case Revenue	2,239,676	2,239,676	2,316,383	3
OPERATING EXPENSES:					
4	Energy Costs	0	0	0	4
5	Other Production	0	0	0	5
6					6
7	Transmission	690	708	708	7
8	Distribution	397,629	408,366	408,366	8
9	Customer Accounts	186,526	192,156	192,156	9
10	Uncollectibles	7,533	7,533	7,791	10
11	Customer Services	0	0	0	11
12	Administrative and General	186,726	191,190	191,190	12
13	Franchise Requirements	13,850	13,850	14,324	13
14	Project Amortization	0	0	0	14
15	Wage Change Impacts	0	0	0	15
16	Other Price Change Impacts	0	0	0	16
17	Other Adjustments	0	0	0	17
18	Subtotal Expenses:	792,953	813,803	814,535	18
TAXES:					
19					19
20	Property	83,417	87,039	87,039	20
21	Payroll	32,194	32,194	32,194	21
22	Business	335	335	335	22
23	Other	0	0	0	23
24	State Corporation Franchise	36,901	31,641	38,357	24
25	Federal Income	211,938	192,529	219,120	25
26	Total Taxes	364,784	343,737	377,044	26
27	Depreciation	416,891	434,919	434,919	27
28	Fossil Decommissioning	0	0	0	28
29	Nuclear Decommissioning	0	0	0	29
30	Total Operating Expenses	1,574,629	1,592,459	1,626,499	30
31	Net for Return	665,047	647,217	689,884	31
32	Rate Base	7,292,186	7,563,858	7,563,858	32
RATE OF RETURN:					
33	On Rate Base	9.12%	8.56%	9.12%	33
34	On Equity	11.23%	10.04%	11.22%	34

For its gas distribution results of operations for estimated 2002, at current rates PG&E predicts an 8.62% rate of return; at proposed rates a 9.12% rate of return. The electric rate increase requested is \$19,480,000. PG&E's authorized gas distribution rate of return is 9.12%, per D.00-06-040. See Table 2.

PACIFIC GAS AND ELECTRIC COMPANY  
2002 ATTRITION APPLICATION  
TABLE 2  
TOTAL GAS DISTRIBUTION  
RESULTS OF OPERATIONS  
(Thousands of Dollars)

Line No.	Description	1999 Authorized At 2000 Cost Of Capital	Year 2000 At Present Rates With Recorded Rate Base	Year 2001 At Present Rates With Recorded Rate Base	Attrition Year 2002		Line No.
					At Present Rates	At Proposed Rates	
		(A)	(B)	(C)	(D)	(E)	
<b>REVENUE:</b>							
1	General Rate Case Revenue	894,394	894,394	894,394	894,394	894,394	1
2	Increase	0	0	(0)	0	19,480	2
3	General Rate Case Revenue	894,394	894,394	894,394	894,394	913,874	3
<b>OPERATING EXPENSES:</b>							
4	Energy Costs	0	0	0	0	0	4
5	Other Production	3,277	3,277	3,277	3,373	3,373	5
6	Storage	24	24	24	24	24	6
7	Transmission	0	0	0	0	0	7
8	Distribution	139,288	139,288	139,288	143,373	143,373	8
9	Customer Accounts	140,827	140,827	140,827	145,072	145,072	9
10	Uncollectibles	3,013	3,013	3,013	3,013	3,079	10
11	Demand-Side Management	0	0	0	0	0	11
12	Administrative and General	98,525	98,525	98,525	101,053	101,053	12
13	Franchise Requirements	13,170	13,170	13,170	13,170	13,457	13
14	Project Amortization	0	0	0	0	0	14
15	Wage Change Impacts	0	0	0	0	0	15
16	Other Price Change Impacts	0	0	0	0	0	16
17	Other Adjustments	0	0	0	0	0	17
18	Subtotal Expenses:	398,124	398,124	398,124	409,079	409,432	18
<b>TAXES:</b>							
19							19
20	Property	23,540	24,584	25,444	26,428	26,428	20
21	Payroll	17,414	17,414	17,414	17,414	17,414	21
22	Business	132	132	132	132	132	22
23	Other	0	0	0	0	0	23
24	State Corporation Franchise	12,222	10,687	9,885	7,908	9,599	24
25	Federal Income	31,913	30,694	28,586	21,634	28,328	25
26	Total Taxes	85,221	83,511	81,461	73,516	81,901	26
27	Depreciation	211,306	213,255	220,418	228,555	228,555	27
28	Fossil Decommissioning	0	0	0	0	0	28
29	Nuclear Decommissioning	0	0	0	0	0	29
30	Total Operating Expenses	694,652	694,890	700,004	711,150	719,888	30
31	Net for Return	199,742	199,504	194,390	183,244	193,986	31
32	Rate Base	2,189,719	2,119,751	2,108,645	2,126,620	2,126,620	32
<b>RATE OF RETURN:</b>							
33	On Rate Base	9.12%	9.41%	9.22%	8.62%	9.12%	33
34	On Equity	11.22%	11.82%	11.42%	10.17%	11.22%	34

**ORA'S Position**

ORA states that PG&E is not automatically entitled to attrition increases between rate cases.

The attrition mechanism is not an entitlement. Nor is it a method of insulating the company from the economic pressures which all businesses experience...Neither the Constitution nor case law has ever required automatic rates increases between general rate case applications. (D.93-12-043, 52 CPUC 2d 471,492.)

In its test year (TY) 1999 general rate case decision, the Commission authorized attrition for 2001, but denied it for 2000. On February 21, 2002, the Commission issued D.02-02-043 granting PG&E a 2001 attrition increase of approximately \$151 million. PG&E's claim that it is entitled to an attrition increase for 2002 is belied by both the substantial magnitude of the \$151 million attrition increase granted by D.02-02-043 and by its ability to manage its system for many years between general rate cases without any attrition increases.

Further, argues ORA, PG&E should not be rewarded with an attrition increase because of a delay of its own making. It was PG&E that requested a delay in the filing of its 2002 general rate case. Therefore, the need for a 2003 general rate case was the direct result of PG&E's election to delay the filing of its TY 2002 general rate case. Having voluntarily delayed a complete review of its cost structure, it should not now be rewarded with yet another attrition increase.



ORA's principal contention is that PG&E's cost structure should be fully reviewed in detail before any further rate increases are granted. In directing the filing of a 2003 TY general rate case, the Commission said:

Developments following the deregulation of the wholesale electricity market have changed utility operations and current rates may no longer reflect PG&E's cost of service. For this reason, it is necessary to review PG&E's revenue requirement to determine if PG&E's rates are just and reasonable. (D.01-10-059, *slip op.*, p.4.)

ORA believes that any further attrition increase contradicts the Commission's observation regarding the need to examine the reasonableness of PG&E's current costs and rates.

## **Discussion**

We deny the attrition increase request. In our review of PG&E's recent rate cases it is apparent that PG&E has not had a full review of its costs since its 1999 general rate case decision D.00-02-046. In that decision, the base year used for recorded costs was primarily 1996, plus some from 1997. (D.00-02-046, *slip op.* 154-160.) In our 2001 attrition proceeding (Application (A.) 00-07-043), we calculated the attrition increase based on 1999 recorded rate base and expense levels adopted in D.00-02-046, plus approximately 3% inflation costs. (D.02-02-043, pp 18-19.)

In D.02-02-043, because of PG&E's unprecedented financial problems, we were uncertain about the actual rate base of PG&E in 2001.

We said:

“... 2001 was an extraordinary year, and PG&E faced unprecedented financial problems. It is reasonable to conclude that PG&E’s financial woes would impact PG&E’s capital spending. PG&E has informed the Commission of efforts to reduce costs such as scaling back of distribution undergrounding work.

“The record before us is insufficient to determine if PG&E’s financial problems resulted in extraordinary reductions in PG&E’s capital spending in 2001, but PG&E should recover its reasonably incurred costs. Therefore, while we approve the increase in capital-related costs stated above, we will make this increase subject to revision downward should PG&E’s actual 2001 capital costs be less than the assumed amount underlying our increase. This will enable PG&E to recover its costs, but protect ratepayers should we determine PG&E’s capital spending was reduced in 2001.” (*Id.* at pp 16-17.)

As of this date we have not reviewed PG&E’s actual 2001 capital costs.

In D.02-04-056, we considered PG&E’s motion for an order ensuring that if, at a later date, the Commission approves an ARA for 2002, the adjustment would be made effective as of the date of the order granting the motion. We granted that motion in D.02-04-056, with an April 22, 2002 effective date.

We said:

1. The *Motion of Pacific Gas & Electric Company (PG&E) for Interim Decision Regarding 2002 Attrition* is granted as set forth below.
2. In the event that the Commission authorizes an ARA for PG&E for 2002, such authorization may be made effective as of the effective date of this Interim Order or such later date as may be determined by the Commission. (D.02-04-056, at p 8.)

In the body of the decision, we made abundantly clear that we were not assuring PG&E that an ARA would be granted.

We said:

We need to allow adequate time for full and fair consideration of whether to approve an ARA for 2002, and if so the parameters and magnitude of such an adjustment.

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We emphasize that we are simply preserving our option to authorize an ARA that could be made effective today. We reserve our right to deny an ARA for 2002 after further consideration. Nothing in today's decision assures PG&E an ARA for 2002. (D.02-04-056 at p. 3, emphasis added.)

After further consideration, we deny PG&E's request for an ARA for 2002. The recorded numbers are too stale and the escalation rates too uncertain to sustain a finding increasing rates by \$96.3 million to meet 2002 costs and rate base. There have been great changes in the economy of California and the United States in the six years since PG&E's last recorded costs were placed on a record before us. There have been even greater changes in the economic status of PG&E. We cannot assume that merely escalating 1996 and 1997 costs and 1999 rate base (at escalation rates that may have no relation to current interest rates) will result in an accurate rendering of PG&E's costs and rate base in 2002. The gap between recorded and estimated is too great.<sup>1</sup> It requires a general rate case to bridge.

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<sup>1</sup> To illuminate the gap it is instructive to compare PG&E's estimated 2001 results of operations with PG&E's 2001 recorded revenues, expenses, and rate base. In Exhibit D to PG&E's application 2001 recorded shows electric department gross operating revenue of \$6.8 billion (as compared to electric department general rate case revenue of \$2.2 billion) and gas department gross operating revenue of \$3.2 billion (as compared to

**Comments on Draft Decision**

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Commission's Rules of Practice and Procedure. Comments were filed on \_\_\_\_\_, and reply comments were filed on \_\_\_\_\_.

**Procedural Matters**

In Resolution ALJ 176-3090, dated June 27, 2002, the Commission preliminary categorized this proceeding as Ratesetting.

**Assignment of Proceeding**

Michael Peevey is the Assigned Commissioner and Robert Barnett is the assigned Administrative Law Judge in this proceeding.

**Findings of Fact**

1. PG&E's recorded costs, other than rate base, have not been fully reviewed by this Commission since PG&E's 1999 general rate case which used 1996 as a base year, plus some costs from 1997.
2. PG&E's recorded rate base has not been fully reviewed since 1999.
3. It is too speculative to base an interim increase in 2002 on such stale numbers.
4. By its own estimate PG&E is currently earning a rate of return of 8.56% on its electric distribution system and 8.62% on its gas distribution system, compared to its authorized rate of return of 9.12% on both systems.

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gas department general rate case revenue of \$.9 billion). PG&E's 2001 recorded rate of return was 12.99%, compared to PG&E's authorized rate of return of 9.12%.

5. PG&E's earnings do not warrant the extraordinary relief of an attrition rate increase.

**Conclusions of Law**

1. PG&E's application to increase electric and gas rates in 2002 to reflect an attrition revenue adjustment should be denied.
2. It is not reasonable to assume that escalating 1996 and 1997 costs, and 1999 rate base (at escalation rates that may have no relation to current interest rates) will result in an accurate rendering of PG&E's costs and rate base in 2002.
3. This order should be effective today to provide certainty to PG&E.

**O R D E R**

**IT IS ORDERED** that:

1. The relief requested in this application is denied.
2. This proceeding is closed.

This order is effective today.

Dated \_\_\_\_\_, at San Francisco, California